

Hearing on Capital Investment in Indian Country

Subcommittee on Financial Institutions U.S. Senate Banking, Housing, and Urban Affairs Committee

Written Statement

**Rodger J. Boyd,
Special Assistant to the Director**

**DEPARTMENT OF THE TREASURY
Community Development Financial
Institutions Fund**

June 6, 2002

CDFI
fund

*Subcommittee on Financial Institutions - U.S. Senate Banking, Housing, and Urban
Affairs Committee; Hearing on Capital Investment in Indian Country -
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**COMMUNITY
DEVELOPMENT
FINANCIAL
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(CDFI) FUND**

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Chairman Johnson, Senator Bennett and Members of the Subcommittee, I am Rodger Boyd, Special Assistant to the Director of the Community Development Financial Institutions (CDFI) Fund. I appreciate the opportunity to appear before you today on behalf of the CDFI Fund. In addition to my current duties as Special Assistant, I served as the lead staff member for the Native American Lending Study conducted by the CDFI Fund. I have been asked to specifically address the findings of that study as they relate to the subject of this hearing, "Capital Investment in Indian Country."

The Community Development Financial Institutions Fund is a government corporation within the U.S. Department of Treasury. The CDFI Fund's mission is to expand the capacity of financial institutions to provide capital, credit, and financial services in underserved markets.

When the Congress authorized the CDFI Fund under P.L. 103-325, the enabling legislation required the CDFI Fund to undertake a study on lending and investment practices on Indian Reservations and other lands held in trust by the United States. The result, known as the Native American Lending Study (the "Study"), was undertaken for the purposes of meeting that Congressional mandate and examining the barriers to accessing capital and providing financial services on Indian Lands¹ and Hawaiian Home Lands^{2,3}.

1 "Indian Lands" are defined for purposes of the Study as lands owned by or under the control of Tribal governments including reservations, Indian Lands, and Alaska Native Villages. For purposes of the Study, Alaska Native Villages have the definition ascribed by 43 USC 1602, et seq.

2 "Hawaiian Home Lands" are defined for the purposes of the Study as trust lands held for the benefit of Native Hawaiian people and are administered by the State of Hawaii's Department of Hawaiian Home Lands.

3 For the purposes of the Study, the term "Native Hawaiian" is defined as "a person having origins in the original peoples of Hawaii", see 62 Fed. Reg. 58,781 (1997). "Native Hawaiian" is not a term that refers to a federally recognized Tribe. Inclusion of Native Hawaiians in the study does not confer or imply any specific, legally enforceable duties on the United States as trustee that apply under certain circumstances when it manages tribal or individual Indian property or resources. In addition, this study does not support or cre-

The Issue

In the Community Development Banking and Financial Institutions Act 1994, Congress found that “[m]any of the Nation’s urban, rural and Native American communities face critical social and economic problems arising in part from the lack of economic growth, people living in poverty, and the lack of employment and other economic opportunities”. Indeed, many communities located in Indian Lands face economic and social challenges that place them significantly behind the rest of the U.S. economy.

Study Approach

The Study was designed to produce a broad, if not necessarily exhaustive, qualitative review of the state of lending and investment on Indian Lands and Hawaiian Home Lands. This was accomplished largely through input from many of the stakeholders involved in capital access issues on Indian Lands and Hawaiian Home Lands. Simultaneously, the Study has attempted to supplement this review with meaningful quantitative input and analysis. This was accomplished through the CDFI Fund’s Financial Survey, the Equity Investment Research Report, and other CDFI Research. Accordingly, the Study approach was designed not only to provide a catalog of economic problems on Indian lands and Hawaiian Home Lands by integrating the concerns and recommendations of those who are attempting to lead their communities into the nation’s economic mainstream, but to provide a statistical reporting as well.

To assist in accomplishing this, the CDFI Fund convened 13 regional workshops and two national roundtable meetings involving Tribal leaders and economic development professionals, Native American and Native Hawaiian business people, private investors and bankers, federal regulatory officials, and federal agency government officials. The Workshops discussed issues related to barriers to capital access and identify possible remedies. The Fund developed this Study approach to gain the knowledge and experience of these participants that have worked with these issues on a day-to-day basis.

The Workshops were complemented by the following research:

- The Financial Survey was administered to 851 Tribal government housing and economic development directors and 735

(Footnote #3 - continued from page 2)

ate any right enforceable or cause of action by or against the United States, its agencies, officers or any person. The CDFI Fund’s experience with CDFIs and prospective CDFIs in Hawaii has suggested that Native Hawaiians face many of the same issues and barriers as Native Americans and Alaska Natives in their attempts to access loans and investment capital. Accordingly, in 1999, the CDFI Fund proposed to Congress to expand the Study beyond the original Congressional mandate to include Native Hawaiians. The Senate Committee on Indian Affairs encouraged and supported the proposed expansion. We do not currently recommend that Congress enact any federal government programs to provide special benefits to Native Hawaiians. The Study addressed various actions that could voluntarily be undertaken by financial institutions and Native Hawaiian organizations. Any program targeting Native Hawaiians as a group is subject to strict scrutiny and of questionable validity under the Constitution.



private financial service organizations (FSOs) located on or near Indian Lands or located in Hawaiian Home Lands to identify the barriers to lending and provide financial services and to help develop recommendations to address those barriers.

- An Equity Investment Research Report on Indian Lands and Hawaiian Home Lands was developed to provide the background and recommendations for enhancing equity capital access. This research included discussions with equity market participants, review of the relevant findings from the Financial Survey, and analysis of the findings from the Workshops. In addition, a questionnaire was administered to participants in the Equity Investment Roundtable that provided useful information about equity investment on Indian Lands and Hawaiian Home Lands.

The CDFI Fund's research found that there exists a significant difference in the amount of capital investment when comparing the rest of the United States to Indian Lands and Hawaiian Home Lands.

The Financial Survey and Equity Investment Research Report found the following evidence of this historic under investment on Indian Lands and Hawaiian Home Lands:

- 65 percent of Native American and Native Hawaiian respondents to the Financial Survey report that conventional mortgages are "difficult" or "impossible" to obtain. Home equity loans and construction and property rehabilitation loans are also in short supply on Indian Lands and Hawaiian Home Lands.
- Business loans were rated as "impossible" to obtain by 24 percent of Native American and Native Hawaiian respondents to the Financial Survey and as "difficult" to obtain by 37 percent. Larger business loans, those over \$100,000, are even more difficult to obtain; 67 percent of said Financial Survey respondents rated them as "difficult" to impossible to obtain.
- 66 percent of Native American and Native Hawaiian respondents to the Financial Survey stated that private equity investments are "difficult" or "impossible" to obtain for Native American and Native Hawaiian business owners.
- 33 percent of Native American respondents to the Financial Survey indicated they had to drive over 30 miles to ATM and bank branches.
- The Equity Research Report estimates the buying power of Native Americans is about \$35 Billion and estimated Indian Country revenue of \$34 Billion for 2001.
- The Equity Research Report estimates that the investment gap between Native American and Native Hawaiian economies and the United States overall totals \$44 billion.

Barriers to Capital Access

The Study identified 17 major barriers to capital access, relating to legal infrastructure, government operations, economic, financial and physical infrastructure, and education and cultural issues.

The Study identified one major barrier to capital access related to legal infrastructure:

1. Uncertain Tribal Commercial Laws and Regulations and the Absence of an Independent Judiciary.

Three major capital access barriers were identified that are related to government operations:

1. Cumbersome, Conflicting, or Ineffective Federal Programs and Regulations.
2. Uncertainty Generated by Changes in Tribal Government Leadership.
3. Poor Understanding of Tribal Sovereignty and Sovereign Immunity.

Five major economic barriers to capital access were identified:

1. Limited Use of Trust Land as Collateral.
2. Inflexible Bank Lending Rules and Regulations.
3. Lack of Capital, Collateral, and/or Credit Histories of Native Americans and Native Hawaiians on Indian Lands and Hawaiian Home Lands.
4. Negligible Economic Base on Indian Lands and Hawaiian Home Lands.
5. Lack of Networking of Native-owned Businesses With Equity Investors.

There are two major capital access barriers related to financial and physical infrastructure:

1. Lack of Financial Institutions on or Near Indian Lands.
2. Lack of Physical and Telecommunications Infrastructure on Indian Lands or Hawaiian Home Lands.

Six major capital access barriers related to education and cultural issues were identified:

1. Lack of Knowledge or Experience With the Financial World on the Part of Native Americans and Native Hawaiians.



2. Lack of Technical Assistance Resources.
3. Failure of Lenders and Investors to Understand Tribal Government or Legal Systems.
4. Historical Absence of Trust Between Tribes and Banks.
5. Differences Between Native American and Native Hawaiian Cultures and Banking and Investor Cultures.
6. Discrimination Against and/or Stereotyping of Native American and Native Hawaiian Communities.

Remedies and Recommendations

Study participants identified a number of potential remedies and recommendations related to the major capital access barriers identified above.

Participants identified one recommendation related to the legal infrastructure barrier cited above.

1. Enhance the Tribal Legal Infrastructure. Some Study participants recommended a strategy of creating a more pro-business legal environment on Indian Lands, through such actions as:
 - Establishment of a Tribal legal infrastructure for business development, including Tribal commercial codes, foreclosure regulations, permitting processes, and general regulatory frameworks,
 - Development of zoning codes and land use plans, and
 - Clarification of sovereignty and sovereign immunity, particularly regarding business and housing development.

Study participants identified four recommendations related to the three government operations barriers.

1. Improve Tribal Planning Processes and Structures.

Some Workshop participants felt that Tribal governments need to enhance their ability to establish, articulate and manage a clear and concise vision, to formulate policies and strategic plans for overall economic development, and to cultivate the professional government workforce necessary to implement such plans.

2. Separate the Goals and Management of Tribal Government From Those of Tribal Business.

Some Workshop participants recommended separating the management of business and government, spinning off Tribally-owned enterprises to a separate bodies for oversight and management, delegating privately-owned enterprise oversight to nonpolitical bodies, and clari-

ifying the differences between Tribal government and corporate liability.

3. Strengthen Tribal Courts. Some actions recommended by Study participants include:

- Increasing the skills and capacity of judges and judicial personnel regarding lender and investor issues, and
- Establishment of enforcement procedures for, garnishment.

4. Streamline and Improve the Efficiency and Effectiveness of Certain Federal and State Programs Used By Native Americans and Native Hawaiians.

Many Workshop participants expressed the need to accelerate the pace of decision-making, reducing excessive requirements and paperwork, rationalizing conflicting requirements and revising programs with overly restrictive entry guidelines, of certain state and federal programs.

There were four remedies identified that relate to economic barriers:

1. Create Alternative Collateral Options for Trust Land.

Workshop participants recommended recognizing and leveraging the value of trust assets; facilitating development of trust land through alternative means of valuation and collateralization, such as the creation of leaseholds and master leaseholds; building equity pools from trust lands and other resources; and converting traditional assets into collateral.

2. Develop New Local and Non-traditional Mechanisms to Deliver Capital on Indian Lands and Hawaiian Home Lands.

Workshop participants suggested that Tribal governments should develop their capacity to orchestrate and leverage all sources of capital, and financial institutions should develop new lending and financing products and revise underwriting criteria to meet the unique needs of Native American and Native Hawaiian markets, including the development of micro-lending programs for small businesses and securitization of oil and gas reserves and timber. Workshop participants proposed two options for providing access to nontraditional sources of debt and equity capital:

- Develop Tribal or Inter-Tribal CDFIs, community banks, and other lending and investment institutions; and
- Create Tribal or Inter-Tribal pools for loan guarantees, equity investments/venture capital, micro-lending and lending for housing and small business.



3. Increase Equity Investment on Indian Lands and Hawaiian Home Lands.

Equity Investment Roundtable participants suggested the following methods of increasing equity investment in Native American and Native Hawaiian communities:

- Create industry sector specific incubators that provide management and technical assistance to start-up businesses and that focus on the specific needs of Native American and Native Hawaiian business owners,
- Use existing “angel investor” networks (i.e. – networks of investors who provide start-up capital for new business, sometimes accompanied by technical expertise and contacts networks),
- Build an “angel” network that specializes in investments in Native American-owned or Native Hawaiian-owned businesses,
- Create community development venture capital (CDVC) funds,
- Use existing corporate venture capital programs,
- Use state and city venture capital programs, and
- Form a public/private intermediary to direct funds into Native American and Native Hawaiian CDFIs, businesses, or projects.

4. Establish a Native American/Native Hawaiian Equity Fund.

To attract equity investments in Native American and Native Hawaiian communities, Workshop participants suggested that the federal government sponsor an equity fund to help encourage private sector investors and public/private partnerships to invest on Indian Lands and Hawaiian Home Lands.

Four recommendations related to the two financial and physical infrastructure barriers cited above, were identified:

1. Increase the Number of Financial Institutions on or Near Indian Lands.

To provide Native Americans and Native Hawaiians greater access to financial services, a number of policies need to be considered, including:

- Creating more financial institutions, including CDFIs, on Indian Lands, and
- Encouraging existing financial institutions that are not located on Indian Lands to open branches on Indian Lands.

2. Develop Regional Financial Institutions.

The Workshop participants believed that regional partnerships and alliances are essential to overcoming barriers to capital and credit access, and possible strategies include:

- Building on partnerships established with the CDFI Fund's regional Inter-Tribal cosponsors and holding follow-up forums similar to those conducted in the Study,
- Establishing information clearinghouses at the regional level on model financing approaches, methods of accessing equity capital, and sources of training and technical assistance,
- Providing channels of information to Native American and Native Hawaiian communities so that they can adapt existing models to their unique cultural and community needs, and
- Establishing regional partnerships among banks, lending institutions, venture capitalists, federal agencies, and Tribes/Inter-Tribal organizations.

3. Develop Financial Products and Services That Will Meet the Needs of Native American and Native Hawaiian Depositors and Borrowers.

Workshop participants suggested that this could be accomplished by financial institutions through the development of new lending and financing products, revised underwriting criteria more suited to the unique attributes of Native American and Native Hawaiian communities, the creation of micro lending programs for small business, and the creation of CDFIs.

4. Create Innovative Strategies to Develop Physical Infrastructure on Indian Lands and Hawaiian Home Lands.

Various initiatives were explored at the Workshops to facilitate development of a more adequate infrastructure system on Indian Lands and Hawaiian Home Lands, including creation of partnerships with private developers to plan for infrastructure development and development of an infrastructure investment strategy that utilizes available federal resources and encourages private partnerships to participate in the funding and development process.

Study participants identified four recommendations related to the seven educational and cultural barriers.

1. Expand Financial Literacy Education Opportunities for Native Americans and Native Hawaiians.

Workshop participants agreed that providing financial literacy education and personal finance education for Native Americans and Native Hawaiians can provide them with the means to participate in the contemporary economy and that culturally appropriate financial literacy curriculum is available from various sources. Many existing CDFIs regularly provide this type of training in their communities.



2. Develop Entrepreneurship Programs for Native Americans and Native Hawaiians.

Workshop participants recommended that these programs include:

- Development of core materials on small business finance and entrepreneurship,
- Establishment of teaching partnerships with Tribal and non-Tribal colleges, financial institutions, CDFIs, and nonprofits,
- Incorporation of web-based training in the curriculum, and
- Facilitation of funding and teacher recruitment through the private sector, Tribes, Inter-Tribal organizations, and federal agencies.

3. Conduct Lender and Investor Education.

Actions recommended by the Workshop participants include:

- Development of informational handbooks on issues such as Tribal government structures, sovereignty and sovereign immunity, and land status,
- Creation of a directory of Tribal credit officers, economic development officers, and department heads and a directory of attorneys qualified to practice in Tribal courts,
- Development of a marketing campaign that illustrates effective practices and success stories, initiation of educational outreach seminars by Native American and Native Hawaiian communities for potential lenders and investors, and
- Initiation of “road shows” focusing on investment opportunities on Indian Lands and Hawaiian Home Lands.

4. Expand Technical Assistance and Training.

From the Workshops, several initiatives were identified for increasing technical assistance and training on Indian Lands and Hawaiian Home Lands:

- Provide Native Americans and Native Hawaiian business owners with technical assistance related to developing business plans and proposals and other business management needs,
- Help Tribal governments develop a comprehensive strategic plan to meet development and financing needs,
- Assist lenders, investors, and potential business partners in developing an understanding of Tribal laws, Tribal enforcement capabilities, and lender rights, and
- Help lenders, investors, and potential business partners understand federal programs, requirements, and application

processes.

Examples of Initiatives and Programs

One of the important aspects of the Study was the identification by participants of programs and initiatives that involve government, the private sector and Tribes to address the major barriers identified above. Each initiative identified below, designed to meet the needs of a particular community, may offer insights to other communities that can be adapted to meet the unique needs of other particular communities or regions.

For example, some Tribes have enacted legislation to promote business development, Tribal commercial codes, land use and planning codes, zoning codes and laws regulating corporate and business activity.

Workshop participants noted that lenders and investors are often reluctant to accept the jurisdiction of Tribal courts to enforce financial contracts and, to address this problem, suggested increasing the capacity of Tribal courts to resolve commercial and financial disputes and to enforce commercial codes. Some initiatives are currently underway:

- The Federal Bureau of Justice Assistance, Department of Justice, and Bureau of Indian Affairs are currently funding technical assistance and training grants for Tribal Court capacity building.
- The National American Indian Court Judges Association has established the National Tribal Justice Resource Center to assist Tribes in strengthening methods of self-government and to provide technical assistance for enhancing Tribal justice systems.
- The Tribal Court Clearinghouse has been created as a resource for Tribal court development, training, court review, code drafting, and training.

To provide Native Americans and Native Hawaiians greater access to financial services, Study participants felt that a number of options need to be considered, including creating more financial institutions on Indian Lands and Hawaiian Home Lands, expanding and/or rebuilding existing financial institutions on Indian Lands, purchasing existing banks, expanding Native-ownership of financial institutions through purchase or de novo creation of new institutions, and creating more CDFIs. Workshop participants and CDFI Fund research identified the following examples of successful initiatives:

- The Cheyenne River Sioux Tribe used an existing revolving loan fund to create the non-profit Four Bands Community Fund, which makes business loans.



- In 1990, the Navajo Nation had only three bank branches and one ATM serving a geographic area of 17 million acres. To increase the availability of financial services on the reservation, the Tribe entered into an agreement with Norwest Bank (now Wells Fargo) to build four new branch banks with ATMs, hire and train Navajo personnel, and target financing to business startups and housing development.
- In all, nine Tribally-owned commercial banks, seven credit unions, and 14 loan funds have been developed nationwide to serve Native American communities.
- Hawaiian Community Assets, Inc. is developing a charter for the first Native Hawaiian-owned bank.
- As of September 30, 2000, the CDFI Fund had made awards totaling nearly \$27 million to 33 CDFIs that provide some level of service to Native American or Native Hawaiian communities.
- In FY 2002, the CDFI Fund initiated its \$5.0 million Native American Technical Assistance program to assist Native American and Native Hawaiian communities in establishing community based CDFIs.

Workshop participants identified regional partnerships and alliances as essential components to overcoming barriers to capital and credit access, and examples of successful regional initiatives include:

- The Native American Development Corporation is a CDFI that provides Native American business communities in Montana and Wyoming with funds to create jobs, develop long-term economic self-sufficiency, and facilitate access to capital. Its Capital Loan Fund was initially capitalized with funding from banks, the federal government, First Nations Development Institute, and private corporations.
- The Native American Lending Group, Inc. is a nonprofit multi-Tribe CDFI in New Mexico that serves 19 Pueblo communities. It was created to provide Tribes, businesses, and individuals access to private investment capital.
- Coastal Enterprises, Inc. is a nonprofit CDFI that serves low-income communities in Maine and provides financial and technical assistance for development and expansion of certain targeted industries, small businesses, housing, and social services. CEI has established a partnership with the Penobscot Indian Nation to develop a CDFI to fund housing and business development.

Tribal leaders and private investors participating in the Workshops suggested strategies that relied on accessing capital sources that have not traditionally been on the Native American investment “radar

screen” and on expanding Native American awareness to include more equity and nontraditional financing and thus increase the likelihood of securing funding.

One example of an existing strategy captured significant Workshop participant attention: Center of North America Capital Fund is an “angel” investor network and investment fund in North Dakota that links two Tribes — the Turtle Mountain Band of Chippewa and the Spirit Lake Sioux — with investors. The CONAC Fund was modeled after Minnesota’s Regional Angel Investor Networks Fund, a series of rural investment funds formed by the Minnesota Investment Network Corporation.

The following are examples of public/private intermediaries cited by Workshop participants that direct funds to Native American and Native Hawaiian businesses:

- The Hopi Credit Association is a Tribal loan fund that provides a bridge between banks and Tribal borrowers, obtaining funds from banks, handling all loan selection and servicing with Tribal members. Participating banks thus gain a point of entry to the Tribal community, via a Tribal loan fund that understands banking needs, and Tribal members are served directly by a credit union that understands their needs.
- Another example is the Southern Ute Growth Fund, which uses a partnership approach and co-invests, using its growth fund and capital provided by outside investors, in a variety of growth opportunities.

Conclusion

Much of the progress in expanding access to capital was not achieved by tribal governments, financial institutions or federal agencies acting alone. Rather, progress often depended on these stakeholders acting together. One of the most important themes to emerge from the CDFI Fund’s research, Workshops, and Equity Research is the need to foster even greater coordinated activity among stakeholders. For example, input of Tribal or Native Hawaiian representatives to any review of the effectiveness of government programs or policies would help to answer questions about community compatibility and relevance. Neither technical assistance nor cultural education will have the desired effect unless Tribes, Native Hawaiian communities, and FSOs commit to such processes. Moreover, FSOs, government regulators, and Tribes would all likely have to participate in attempts to create new loan products and equity investment opportunities for Native American or Native Hawaiian communities.

